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No. 7604

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

WISE MANUFACTURING COMPANY (a corporation),

Appellant,

vs.

E. W. OLIN, RALPH SITES and BERKELEY PATTERN WORKS,

Appellees.

BRIEF FOR APPELLEES.

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BRIEF FOR APPELLEES.

I.

INTRODUCTION.

This action was brought by appellees Olin, Sites and Berkeley Pattern Works, creditors of appellant, Wise Manufacturing Company, having provable claims against appellant, in excess of $500.00, to have Wise Manufacturing Company adjudicated a bankrupt.

The original petition was filed March 30, 1933, prior to actual knowledge of the concealment of certain assets and the actual details of another asset later charged, and alleging only the sale of certain assets consisting of tools and equipment and the use of the

proceeds to prefer certain creditors and the abandonment of the business and dissipation of assets to the injury of creditors.

The amended petition was filed June 7, 1933, repeating the allegations of the original petition as to the sale of the tools and equipment, but further alleging the appellant's concealment of the proceeds therefrom in a certain bank account with the intent to hinder, delay and defraud its creditors. The amended petition further charges the concealment of a certain contract, dated February 27, 1930, and the assets to the bankrupt constituted thereby. It does not mention two later modifications of that contract, the existence of which was not known by petitioners at the time of filing the amended petition.

The Honorable A. F. St. Sure, sitting in the United States District Court, heard the case and adjudicated Wise Manufacturing Company a bankrupt, finding: (1) That the proceeds of the sale of the tools and equipment had been concealed, by appellant having deposited them in a bank account in the name of an employee; (2) That the contract of February 27, 1930, and the two modifying contracts, offered in evidence by appellant, in support of its contention that the consideration provided by the original contract had then in part ceased to exist, and the rights flowing to appellant from, or pertaining to the original and modifying contracts, were assets of appellants; (3) That the said contracts, the assets constituted thereby and arising therefrom, and possible causes of action arising therefrom, were concealed by appel-

lant; (4) That the transactions by which the concealments were effected were also concealed; (5) That the concealment of the contracts, the assets constituted thereby, the transactions by which the concealments were effected and the said possible causes of action, were kept concealed, and creditors and stockholders actively misled, by certain false representations with regard thereto; (6) That these concealments were with the intent to hinder, delay and defraud creditors; (7) That the concealments continued from the time of their commission and were not discovered up to within four months of the filing of both the original and amended petitions; and finally, (8) That the transactions described are *tainted with fraud and concealment and warrant a full and complete investigation through the processes of the Bankruptcy Court.*

This appeal is neither based upon a contention that appellant is not bankrupt, nor upon any contention that it has not concealed its assets. On the contrary, it admits, in substance, that a conspiracy to defraud has been proven, but claims appellees should have uncovered the fraud sooner, and that, since, of the assets concealed, one of them, the bank deposit, has now disappeared (although this is not proven), or had become difficult to realize upon, and since another, the contract, has been modified as to consideration, the concealments do not warrant the adjudication.

In the final analysis, appellant is here attempting to resist investigation and resort to the processes of the

Bankruptcy Court, which the District Court felt should be had, in order to continue to deprive its creditors of their due. It was strenuously maintained at the trial, and here, but not so obviously, that the corporation has no assets and, therefore, that it would be useless to order an adjudication. Appellant is making a very determined and costly fight to keep this company out of bankruptcy, which seems rather inconsistent with the claim that it has no assets.

Appellees' position is that the facts warrant the adjudication, that they neither knew, nor were chargeable with knowledge of the concealments prior to the four months' period, that a Trustee in Bankruptcy is the proper party to realize on the bankrupt's assets, that appellees should not be obliged to assume the entire burden of uncovering and bringing in those assets alone, when the benefits thereof will be available to all creditors alike, and that denial of resort to the processes of the Bankruptcy Court might result in perpetuation of the fraud and concealments already proven and found.

II.

DRAMATIS PERSONAE.

Our efforts being to clarify the facts of this case, in the belief that an affirmance of the adjudication of the court below will follow upon the facts being clearly brought to this court's attention, we set forth, for the convenience of the court the names and a brief description of the persons herein involved or mentioned.

The object of these descriptions will be, in part, to aid the court to follow the references in both briefs to the various persons involved, and in part, to clarify and correct the haphazard statement of the case and statement of facts contained at scattered places in appellant's brief,* in other words to fulfil the functions of a counter statement of facts.

Wise Manufacturing Company: Respondent below, appellant here. A California corporation which, by contract, had taken over the assets and assumed the liabilities of Standard Die & Tool Company, Inc. Its stock was all common, 4670 shares of which were held by Standard Die & Tool Company, Inc., and 271 shares by others. All of this outside stock was later bought up by Wise with money derived from the transfer of the corporation's patents.

Standard Die & Tool Company, Inc.: An inactive California corporation which had sold its patents and its other assets (although the assignment was never formally made) to Wise Manufacturing Company. 660 out of a total of 694 shares of its common stock was held by Roy T. Wise. Of its preferred stock, 5 shares were held by Roy T. Wise and the remaining 258 by others. All of the outstanding common and some of the outside preferred stock was later acquired by Wise with money derived from the transfer of the patents of Wise Manufacturing Company.

Wise Patent and Development Company: A Delaware corporation formed by Wise, Hays and Diehl to

*A perusal of appellant's brief will disclose to the court the numerous other matters wherein its brief fails to comply with the Rules of Court.

take over the patents of Wise Manufacturing Company for a consideration of $75,000.00, which consideration was subsequently reduced by the modifying contracts. The later contracts were brought to the attention of the petitioners and appellees for the first time with the filing of the answer. This corporation was owned and controlled entirely by Hays, Wise and Diehl at all times, as was Wise Manufacturing Company controlled by Wise alone. For this reason there is a possibility that these modifying contracts were manufactured after the event, and appellees are justified in so asserting, in the light of other evidences of fraud and criminal acts, both amply proven at the trial.

Roy T. Wise: Promoter and inventor. President of, and a director, and in control of Wise Manufacturing Company and Standard Die & Tool Company, Inc. Also holder of one-third of the stock in Wise Patent and Development Company. It was Wise who contacted Hays and Diehl and made the contract of February 27, 1930, by which the patents were transferred outright to Wise Patent and Development Company in consideration of $75,000.00, at a time when a contract with Westinghouse Electric & Manufacturing Company was available by which $100,000.00, in addition to royalties, was to be paid for one year's use of the patents.

Pansy Wise: Wife of Roy T. Wise. Officer, director and stockholder of Wise Manufacturing Company and Standard Die & Tool Company, Inc.

Edward W. Olin: Shop foreman (and a dummy director) of Wise Manufacturing Company. He is one

of the petitioning creditors here and at one time brought a suit against the appellant upon a labor claim, being represented in that action by Mr. Waddell.

Ralph Sites: One of the petitioning creditors, formerly a workman in Wise Manufacturing Company's shop and who one time brought a suit against the company upon a labor claim, being represented therein by Mr. Waddell.

Berkeley Pattern Works: One of the petitioning creditors.

Huldur Jacobsen: Personal secretary and stenographer to Wise, in whose name a bank account was opened to deposit the proceeds of the sale of tools and equipment of the Wise Manufacturing Company, not, it is claimed by appellant to defraud or cheat creditors, but merely with the view to preventing attachment of the funds by creditors, which hiding of assets, appellant claims is no departure from the secrecy and privacy with which an individual is entitled to transact his business. (Appellant's Brief p. 10.)

Will H. Hays: Sullivan, Indiana, and Beverly Hills, California, capitalist, attorney at law, moving picture magnate, promoter, and one of the combination who formed and financed the formation of Wise Patent and Development Company, acquired one-third of its stock and financed the acquisition of the patents by it, after first securing the much more favorable contract from Westinghouse Electric & Manufacturing Company, all with the knowledge of but one of the stockholders of Wise Manufacturing

Company, namely, Wise. In the arguments before the District Court counsel for respondent, appellant here, described Hays as the reason back of the resistance to the adjudication of Wise Manufacturing Company as bankrupt, in the following phrase: "Mr. Hays would not like it".

Diehl, Ambrose N.: Diehl, president of the Columbia Steel Company, subsidiary of the Bethlehem Steel Corporation, and the contact man with Westinghouse Electric & Manufacturing Company, and one of the participants, to the extent of one-third of the stock in Wise Patent and Development Company in the profits to be derived from the patents of Wise Manufacturing Company.

Alonzo C. Owens: Law partner of Hays in Sullivan, Indiana, who handled in behalf of Hays the financial and other details of the various transactions between Hays, Diehl, Wise, and Wise Patent and Development Company. It was to Alonzo C. Owens that a note and mortgage was given for $25,000.00 upon the assets of Wise Manufacturing Company to secure the repayment of $25,000.00 advanced by Hays to pay off certain creditors and some stockholders. This is the same $25,000.00 that Wise falsely represented he received for the patents. The deal was handled in Owens' name to keep the name of Hays out of the picture.

The Unholy Three: Roy T. Wise, Will H. Hays and Ambrose N. Diehl.

This was simply an appellation which sprang into being for the first time at the trial, upon the realiza-

tion of the unrighteousness of the transactions of these parties, and, particularly, that portion of the contract of February 27, 1930, which permitted a portion of the $75,000.00 consideration for the patents to be used by Wise to freeze out the balance of the stockholders in the California companies, so that they would not participate, even to a small extent, in the profit to be derived from the $75,000.00 consideration. Appellant's brief attempts to claim that Hays, Diehl and Wise were being referred to as "the unholy three" prior to the trial and to argue therefrom that appellees must have had knowledge or means of knowledge of the illegal transaction at a much earlier date. This, however, was not the case.

Palm: Franklin C. Palm, professor of history at the University of California, one of the holders of preferred stock in Standard Die & Tool Company, Inc. On November 30, 1931, Professor Palm, in his own behalf and as attorney-in-fact for various stockholders of Standard Die & Tool Company, Inc., brought suit against Diehl, Hays, Wise and Wise Patent and Development Company in the United States District Court, Northern District of California, to compel payment to plaintiffs of the full par value of their stock, or to require Wise, Diehl, Hays and Wise Patent and Development Company to retransfer the patents to the California companies. At the time this suit was brought, Professor Palm was, with others, under the impression that $25,000.00 had been received by Wise Manufacturing Company for the patents. Appellant here seeks to charge petitioners with knowledge of all of the transactions and con-

tracts between Hays, Diehl, Wise, Wise Patent and Development Company and Wise Manufacturing Company, by reason of the fact that this suit was a matter of public record and by reason of the fact that the attorney for Professor Palm in that case was also the attorney for two of the petitioning creditors, namely, Olin and Sites, in a Justice's Court action on labor claims against the Wise Manufacturing Company.

Halsey J. White: An employee of the American Investment Company, an affiliate of the Bank of America in Berkeley. He was employed by Wise to dispose of part of the $30,000.00 of preferred stock of the Standard Die & Tool Company, Inc., and sold some of it to his customers in the bank. He was also a preferred stockholder in Standard Die & Tool Company, Inc. Mr. White was paid the sum of $1000.00 by Hays over and above the repayment to him of the face value of his stock, in consideration of his refraining from insisting on getting the facts concerning the transfers of the patents. As unofficial representative of a number of other preferred stockholders, he had made inquiries concerning the details of the transfer and what had become of the patents and what consideration, if any, was paid therefor. It was to White that Wise stated he was not at liberty to disclose the information.

Mr. Sorrick: Manager of the Bank of America at Berkeley, who was told by Mr. Eltse, of Clark, Nichols Eltse, not to give any information concerning the $25,000.00 transaction, as one of the conditions of the

pay-off of certain creditors and stockholders was that the terms of the deal and the parties involved were not to be discussed or revealed.

Douglas F. Scott: The trust officer of the Bank of America at Berkeley, who handled escrow 167, through which money was paid by Hays to buy up all of the outstanding common stock of the Wise Manufacturing Company and the outstanding common and some of the preferred stock of Standard Die & Tool Company, Inc., and also to pay certain of the creditors.

Waddell: James Waddell, attorney at law, one of the attorneys for Palm in his suit in behalf of stockholders against Hays, Wise, Diehl and Wise Patent and Development Company. George F. Sharp was the other attorney, but he does not enter into the picture here. Waddell was also attorney for Olin and Sites at one time in the above-referred to labor claims suit. He was also attorney for and director of Wise Manufacturing Company. Although nothing appears in the record to the effect that Waddell had any knowledge of the concealments or fraudulent transactions involved in this case, appellant seeks to charge appellees with knowledge supposed to be had by Waddell because he drew the complaint for Palm, and because at one time he was attorney for two of the appellees here, in a different matter, and because of inferred possibility of knowledge gained by reason of his representation of Wise Manufacturing Company as director and attorney.

N. W. Dobrzensky: Attorney for Will H. Hays, but not of record in any capacity in this action.

Clark, Nichols & Eltse: Attorneys of record in this proceeding for Wise Manufacturing Company. Mr. Eltse, of this firm, was attorney for and director of Standard Die & Tool Company, Inc., arranged Escrow 167, and gave instructions that no information was to be given out concerning it. It was Mr. Eltse, also, who sent out the letter to stockholders of Wise Manufacturing Company and Standard Die & Tool Company, Inc., urging them to turn in their stock, intimating that creditors of the companies might take action which would cause the stockholders loss, although, at the time, all of the creditors had been paid off through Escrow 167.

F. W. Peters: Present attorney for Franklin C. Palm and other preferred stockholders of Standard Die & Tool Company, Inc. Mr. Peters was substituted for Mr. Waddell in the case of *Palm v. Hays, et al.,* on February 6, 1933, Professor Palm being dissatisfied with the lack of progress being made by Mr. Waddell and his failure to develop sufficient facts to proceed beyond the filing of the complaint in that action. It was Mr. Peters who developed the history of the transfer of the patents and of the Hays, Diehl and Wise transactions, and from whom petitioning creditors, on or about March 30, 1933, received their first information as to these concealments of assets and fraudulent transactions.

Floyd B. Cerini: Attorney for the petitioning creditors, and who initiated this proceeding. It was to Mr. Cerini that Mr. Peters disclosed the information as to the concealment of assets by the appellant, and

Mr. Cerini accompanied Mr. Peters on some of his later visits to Mr. Wise. Mr. Cerini associated Resleure, Vivell & Pinckney and Eugene R. Elerding herein shortly prior to the trial.

III.

ARGUMENT.

1. REFUTATION OF APPELLANT'S POINT I, THAT THE CONCEALMENT OF THE BANK DEPOSIT WAS NOT GROUND FOR ADJUDICATION IN BANKRUPTCY BECAUSE: (1) THERE WAS NO INTENT TO CHEAT OR DEFRAUD CREDITORS, MERELY TO HIDE ASSETS FROM THEM; AND (2) THE OBJECT OF THE CONCEALMENT HAD DISAPPEARED PRIOR TO THE 4 MONTHS PERIOD.

(a) Concealment of assets to prevent creditors from attaching is an act of bankruptcy.

It is obvious from the statements in appellant's brief that the bank deposit transaction constituted concealment with intent to hinder and delay creditors, if not to defraud them.

Wise sold certain tools and equipment of Wise Manufacturing Company for $612.00, or thereabouts, and with the avowed intention of preventing creditors from attaching the fund, placed the proceeds in a bank deposit in the name of his secretary and stenographer, Miss Huldur Jacobsen. So far proof is supplied by a stipulation of the parties made in open court (75-81). It was also stipulated that Huldur Jacobsen took the money and the Company has never been able to collect it, and that $184.85 of the fund went to pay attorney's fees. It is claimed, but neither

proved nor stipulated, that the balance of $345.55 went to pay Huldur Jacobsen for prior salary. It is not claimed even that the salary was for services of a recent date.

Appellant, with refreshing naiveté, states that it does not concede that such *hiding of assets* is an act of bankruptcy, unless the intent is to *defraud or cheat* creditors. Appellant admits, however, that the transaction is a technical concealment with a view to hindering, delaying and defrauding creditors, but claims that this is not a departure from the secrecy and privacy with which any individual is entitled to transact his business. The Bankruptcy Act, however, shows on its face that intent to defraud is not necessary because the words "hindering, delaying or defrauding" are set forth in the disjunctive. The statute reads,

> "Acts of Bankruptcy by a person shall consist in his having:
>
> (1) Conveyed, transferred, concealed or removed, or permitted to be concealed or removed, any part of his property with intent to hinder, delay OR defraud his creditors, or any of them."

We can hardly conceive a situation whereby a creditor can be more hindered or delayed than by hiding assets so that he cannot attach them.

Appellant cites no authority for his position that there must be actual intent to defraud creditors as well as hindering or delaying them, from which we infer that as to this transaction the act of bankruptcy is shown.

In 7 *Corpus Juris,* at p. 50, the words, "intent to hinder, delay or defraud" are defined as follows:

> "Such intent involved a purpose wrongfully or *unjustifiably* to prevent, object, embarrass or postpone creditors in the collection or enforcement of their claims, and may be inferred from the natural and necessary result of transfer."

In *In re Hughes,* 183 Fed. 872 at 874, the issue is fully and clearly determined in the following language:

> "The question, therefore, is whether this was a conveyance 'with intent to hinder, delay, *or* defraud' creditors, or any of them. The statute is in the disjunctive, and while it may be admitted, and is I think true, that the words 'hinder' and 'delay' are synonymous (Read v. Worthington, 9 Bosw. (N. Y.) 628), it is not necessary, on the language of the statute itself, that any intent to defraud should be present. It is enough if any creditor is intentionally to be hindered or delayed. If the intent to hinder and delay exists, a conveyance made by an embarrassed debtor with a view, known to the purchaser, of securing the conveyed property from attachment, is voidable as against creditors, even though it be honestly made, and the debtor intends, as Hughes says he did, that all creditors should be paid in full. Kimball v. Thompson, 4 Cush. (Mass.) 446, 50 Am. Dec. 799. This must necessarily be the correct view upon any consideration of language which traces its origin to the statute of Elizabeth; for a debtor's property is in legal theory subject to immediate process at the instance of any creditor, and a debtor will not be permitted to hinder or

delay any creditor by any device which leaves his property, or the avails of it, subject to his control and disposition; and it makes no difference that the debtor intends to apply the avails of the same to the payment of his debts. It still remains true that he has hindered his debtors from applying the property in the way that they have a legal right to rely upon."

(b) Concealment is a continuing offense and lasts up to the time of discovery and does not cease to be a concealment when the property itself ceases to exist.

The only two cases dealing with the duration of the act, definitely hold that the concealment continues up to the time of its discovery, and if not discovered until within four months of filing of petition for adjudication in bankruptcy, even though committed prior to the four months period, it nevertheless continues as an act in bankruptcy. Thus in *Citizens' Bank v. W. C. De Pauw Co.,* 105 Fed. 926 at 930, Grosscup, Circuit Judge, delivered the opinion of the court, as follows:

"* * * It may, perhaps, with correctness, be said that the separation of some tangible thing, money, or chose in action, from the body of an insolvent debtor's estate, *and its secretion from those who have a right to seize upon it for the payment of their debts, is, within the law, a concealment, and continues such as long as the secretion remains.* In such case, the property open to creditors is decreased by just the amount thus secreted. It is, to all intents and purposes, so far as the creditors are concerned, as if the property thus secreted had not been in existence. There is nothing to put the creditors upon notice; nothing

that they may keep within their vision—a tangible subject of inquiry, either as to its value or its ownership. It is, in effect, a concealed withdrawal from possibility of seizure of just so much of the debtor's estate."

In *In re Havens,* 255 Fed. at 478, 481, the Circuit Court of Appeals for the Second Circuit says:

"* * * *The concealment of property* made an act of bankruptcy by section 3 *may be a continuing concealment and the four months period may run from the date of discovery.* Citizens' Bank v. De Pauw Co., 105 Fed. 926, 45 C. C. A. 130. It was, we think, clearly the intent of the pleader to allege a continuing concealment, not discovered until within four months of amendment."

Appellant admits that the act of concealment continues up to the time of discovery, but contends that because the bank deposit here was all used up and paid out in 1931, the subject matter to which the act of concealment relates, had ceased to exist and that the act of concealment could not continue after such cessation of existence. Appellant cites two cases, *Citizens' Bank v. De Pauw Co.,* 105 Fed. 926, and *Ruthers v. U. S.,* 9 Fed. (2d) 496, for this second of its naive contentions. Neither of these cases is, we submit, even remotely in point.

The law on the subject is exactly contrary to appellant's contention. Thus in *Kalin, et al. v. United States,* 2 Fed. (2d) pp. 58-59, the Circuit Court upheld the following charge to the jury:

'Now, I charge you that, in order to constitute a fraudulent concealment, *it is not necessary that*

the money should be retained for their own use for any indefinite or definite time, but if they knowingly and if they fraudulently kept away from their trustee in bankruptcy any of their assets and used it for the purpose of their own benefit or for the purpose of benefiting some other person, not merely paying a creditor as against another in anticipation of bankruptcy, *but if they fraudulently concealed from the trustee in bankruptcy the fact of having the assets and the assets themselves and used it either for their own benefit or for some one whom they selected to prefer or to be a beneficiary of it, they would be guilty in either event.*' "

In *United States v. Knickerbocker Fur Coat Co.*, 66 Fed. Rep. (2d) 388 at 390, the Circuit Court of Appeals for the Second Circuit says:

"* * * *And the crime is complete when the act of concealment or transfer is performed with a criminal intent.*"

While these two cases were, like the second of the cases cited by appellant, brought under the criminal statute, the principle, that the act is complete when the concealment is made or the transfer performed, regardless of the non-existence, or later destruction or alienation of the asset, is the same. Moreover, there is no proof that the property in question had ceased to exist. The stipulation upon which appellant so confidently relies to supply its defect in proof, expressly excluded any stipulation as to the disposition of the money, and the furthest the stipulation went was to agree that Huldur Jacobsen took the money

and that the company has never been able to collect it, and that Clark, Nichols & Eltse got $184.85 on account of attorney's fees.

We quote from the transcript of record at page 80:

> "Mr. Resleure. All right. We will stipulate to everything that Mr. Clark says, except we won't stipulate that the $345.55 went to pay prior salary. You can testify, yourself, as to that.
>
> Mr. Clark. * * * She took the money, we never have been able to collect it.
>
> Mr. Resleure. All right, we will agree to it.
>
> Mr. Clark. And will you stipulate we got $184.85 on account of attorneys' fees?
>
> Mr. Resleure. Yes."

There is nothing in the stipulation to show that the balance of the fund has disappeared, and it would make no difference if it had. If appellant's theory were correct, then an insolvent debtor could hide his assets, thereby preventing their attachment by creditors, and later, beyond the four months' period, destroy those assets and thereby accomplish a defeating of the provisions of the Bankruptcy Act.

The law is well settled that all that is necessary to constitute the defendant a bankrupt is that he owes debts; it is not necessary that he has assets.

> *Vulcan Sheet Metal Co. v. North Platte Co.*, 220 Fed. 106;
>
> *In re J. M. Ceballos*, 161 Fed. 445;
>
> *In re Hirsch*, 97 Fed. 571.

From this statement of the law it is obvious that a later destruction of assets would not cure a prior con-

cealment, otherwise the points decided by the above decisions would be academic only.

Appellant contends that because the words "was an asset" are used in the findings instead of the words "the money deposited *is* the property of the corporation", that appellees have adopted the theory contended by appellant that if the money is no longer the property of the corporation, there is no act of bankruptcy. This is not appellees' position. Furthermore, the attempt to secure a stipulation as to the later fraudulent transfer or preference of the property concealed, does not cure the earlier concealment. Even had appellant accepted appellees' invitation to prove this, it would not have helped appellant's case. As a matter of fact, Roy T. Wise and Huldur Jacobsen were discreetly kept from the stand throughout the entire trial. The whole point is that we pleaded and proved a concealment, and there is no variance shown, simply because a later fraudulent disposition, unknown to petitioners, is attempted to be set up.*

*This fully answers appellant's Point III, that appellees pleaded a consideration under the contract of February 27, whereas there proved and the court found an amended consideration under the modifying contract. For this reason that portion of appellant's brief will not be further treated.

2. REFUTATION OF APPELLANT'S POINT II THAT THE CONCEALMENT OF THE CONTRACT OF FEBRUARY 27, 1930, AND THE ASSET CONSTITUTED THEREBY WAS NOT AN ACT OF BANKRUPTCY WITHIN THE FOUR MONTHS PERIOD, BECAUSE: PETITIONING CREDITORS SHOULD HAVE KNOWN ABOUT IT SOONER; THE CONSIDERATION PROVIDED IN THAT CONTRACT WAS CHANGED; AND ALL OF THE CONSIDERATION FOR THE CONTRACT WAS NOT PAID, DUE TO FAILURE IN PART OF THE DEAL WITH THE WESTINGHOUSE ELECTRIC MANUFACTURING COMPANY BY REASON OF DELAY WHILE THE "UNHOLY THREE" WERE TRYING TO GARNER IN THE LAST OUNCE OF PROFIT FROM THE FRAUDULENT TRANSACTIONS.

(a) Concealment may be a continuing act and, in this case, the contract of February 27, 1930, the modifying contracts and the assets constituted thereby were actively concealed until March 30, 1933.

The evidence in the case was clear, convincing and definite that the first knowledge that petitioning, or any, creditors received, as to the Hays, Diehl and Wise transactions, and the existence of the contract of February 27, 1930, was obtained through the investigation made by F. W. Peters, in his capacity as attorney for Franklin C. Palm, a shareholder of Standard Die & Tool Company, Inc. The existence of the modifying contract was not known until the answer herein was filed.

Fred W. Peters stated he did not receive the contract of February 27, 1930, until February 23, 1933, about three months after he first contacted Mr. Wise, and that he knew when petitioning creditors first became acquainted with the existence of this contract, because he told Mr. Cerini, who represented the creditors, about the contract next day, February 24,

1933, but did not show him the contents until two weeks later (63).

Floyd B. Cerini, one of the attorneys for the petitioning creditors, stated that in a conversation with Mr. Wise and Mr. Peters, about the first week of March, 1933, Mr. Wise stated he did not want the contract disclosed to any one, that very few people knew of it, and that he did not want Mr. Dobrzensky to know that Mr. Peters had seen the contract. Mr. Cerini further stated that that was the first time he learned about the contract and that, a week or two later, he imparted knowledge of the contract to his clients (82, 83).

Mr. Douglas F. Scott, trust officer of the Bank of America, testified that even the details of Escrow 167, through which certain creditors and stockholders received payment, was kept secret, that he had received a letter from Ralph R. Eltse reading in part, "we solicit confidence as to all matters contained in this letter", and that Scott observed confidence in regard to the escrow and nobody knew of any of the matters contained in it (132).

Halsey J. White did not know that the patents were being transferred, although he seemed to have been more active than any one else in uncovering the facts. He was the last of the common stockholders to take down the money that was put up for the common stock (150), and he was paid $1000.00 in consideration of his refraining from insisting on getting the facts as to the transfers and that that was the real and true

consideration (152). This consideration, paid to aid and assist in keeping the transactions secret, was paid by Mr. Hays (148).

In order to mislead creditors and others as to the existence and details of the contracts, Wise falsely represented that he had received $25,000.00 for the patents (70, 96, 126, 162). This was the same $25,-000.00 which Hays had loaned to the company, through Alonzo Owens, and for which Hays received, in the name of Owens, a note and mortgage and certain of appellant's assets.

It is contended that as Waddell was attorney for the petitioning creditors, and for Franklin C. Palm in his suit against Hays, Wise, Diehl and the Patent Development Company, the petitioning creditors are charged with knowledge which Waddell may have had. In the first place, an examination into the nature of Waddell's representations of Olin and Sites, two of the petitioning creditors, discloses no reason why he should or would have given them any information, even if he himself had knowledge of these facts with regard to the concealment of the contracts. Waddell was attorney for these two petitioning creditors only in a Justice Court action against Wise Manufacturing Company upon certain labor claims (168). In the second place, an examination of the complaint in the suit of Palm against Hays, et al., discloses no knowledge on the part of Waddell as to the contracts. On the contrary, it discloses an almost entire lack of knowledge (87-94). The suit in question simply prayed

that defendants should pay the plaintiffs the full par value of their stock or that the Wise Patent and Development Company retransfer the patents to Standard Die & Tool Company.

The complaint in Palm's suit is significantly silent as to the details of the transfers and shows complete lack of knowledge of the true facts. Thus it says that on March 5, 1930, Wise, by reason of his control of Wise Manufacturing Company and Standard Die & Tool Co., Inc., caused all the assets and business of these corporations to be transferred to Wise Patent and Development Company (91). It says nothing as to the nature of the transfer, the consideration therefor, the contract between Hays, Diehl and Wise, nor the existing deal with the Westinghouse Electric & Manufacturing Company. It is not credible that Waddell could have known of these matters and not helped them.

Moreover, even had Waddell actual knowledge of the facts in question, his representation of Wise and of Wise Manufacturing Company would have sealed his lips to other clients. Furthermore, there is no proof that he divulged such information to the creditors, if he had it. The proof is that the creditors did not have any information.

Appellant contends that Palm knew when he filed his suit in November, 1930, that Wise was lying when he represented that $25,000.00 was the sale price of the patents and intimates that Mr. Peters did not believe this was true. Appellant is again refreshingly naive when it cites authority for the proposition that:

> "When a lie is discovered, you can no longer accept the statements of the liar and you are charged with notice."

From this statement of the law, appellant argues, that, since a clue to the fraud or concealments was available to appellees, which if diligently followed up would have led to a discovery of the full and true facts, they were chargeable with knowledge of the entire situation.

We have no quarrel with the authorities cited by appellant in support of this contention, except that they deal with statutes of limitation and not with the four months period prescribed by the Bankruptcy Act. We do dispute, however, appellant's premises.

In the first place, the clue was extremely slight and the trail effectively covered by appellant's active false representations. Moreover, it was the stockholders and not the petitioning creditors who became suspicious, and there is no evidence in the record to the effect that they divulged their suspicions or any clue that they might have had to the petitioning, or other, creditors. Moreover, these stockholders who became suspicious or, as appellant puts it, had a clue to appellant's wrong doing, did exercise all due diligence in attempting to thrust aside the veil of secrecy and concealment surrounding the transactions. They did what they could. They employed Waddell to investigate. When Waddell gave them no satisfaction or results, either by reason of the fact that he could uncover nothing, or because he ran into a situation as to which his lips were sealed on account of his dual

representation of Palm and the Wise Manufacturing Company, they employed Mr. Peters. It took Mr. Peters almost three months of constant effort to get Wise to speak, and no one examining the record will claim that Peters was not a diligent investigator. Furthermore, all the knowledge and all the information was in the control of Hays, Diehl and Wise, and they guarded their secret well. There is nothing in the record to show that Wise would have been ready to talk until after three months of constant pressure from Mr. Peters. The evidence is that he did not talk till then. The burden is on appellant to show he would have talked sooner.

The law does not require an unreasonable standard of diligence, even after suspicions are generated or a clue discovered, but merely requires that diligence which a reasonable man would exercise under the circumstances. The law, furthermore, will not seize upon some small circumstance to show that a person has not discovered the fact that he has been cheated soon enough, in order to deny relief to such a person who has been plainly shown to have been defrauded. Thus Judge Olney, in *Victor Oil Co. v. Drum,* 184 Cal. 226, 241, said:

> "Without some information which carried a direct implication or suggestion of possible fraud, the plaintiff could not be put upon inquiry. The courts will not lightly seize upon some small circumstance to deny relief to a party plainly shown to have been actually defrauded against those who defrauded him on the ground, forsooth, that he did not discover the fact that he had been

cheated as soon as he might have done. *It is only where the party defrauded should plainly have discovered the fraud except for his own inexcusable inattention that he will be charged with a discovery in advance of actual knowledge on his part.*"

In any event, neither the petitioning, nor any other, creditors had any knowledge, information, clue or suspicion of these contracts or the concealment of the assets represented thereby until Mr. Peters took Cerini into his confidence about March 30, 1933.

(b) The authenticity of the modifying contracts is not definitely established, but at best, these contracts merely diminished the consideration, and they still constitute an asset to appellant which was effectively concealed, and knowledge thereof was not developed until appellant's answer to the petition was filed.

Appellant contends that because the $75,000.00 consideration provided for in the contract of February 27, 1930, was cancelled and a new contingent consideration substituted therefor, petitioners' cause of action to adjudicate appellant a bankrupt, falls.

We do not admit the validity or authenticity of these modifying contracts and submit that "The Unholy Three" were not incapable even of manufacturing these contracts *ex post facto,* to prevent their transactions from being investigated by the Bankruptcy Court.

Furthermore, there was no valuable consideration for the alleged modifications in the selling prices of appellant's patents. Hays, Diehl and Wise had no

warrant to deprive the Wise Manufacturing Company, its stockholders and creditors, of the benefits of the earlier contract, just because, in their greed to secure the last ounce of profit from their fraud, they postponed closing the deal with Westinghouse Electric & Manufacturing Company until such time as they could freeze out the other stockholders, and thereby failed to close their deal until the beginning of the recent economic depression. It is true that the value of the patents was reduced by general economic conditions and that Westinghouse Electric & Manufacturing Company insisted, the deal not having been promptly closed, on a reduction in their terms of payment. This, however, was a chance that Hays, Diehl and Wise took when they delayed closing with Westinghouse in order to have time to eliminate the other stockholders. It is just another evidence of their bad faith, that, having lost by their delay, they sought to have appellant and its stockholders and creditors absorb the loss.

The foregoing, however, is largely beside the point. If the modifying contracts are not authentic or if they are invalid by reason of lack of consideration, then the act of bankruptcy consists of having concealed the contract of February 27, 1930. If, on the other hand, the modifying contracts are valid and authentic, the act of bankruptcy consists of concealing them and the assets they represented.

It is not disputed that there was, and still is, money coming from Wise Patent and Development Company, even under these modifying contracts, nor that Wise Patent and Development Company is still receiving

royalties from Westinghouse Electric & Manufacturing Company, wherewith to pay its creditors after advances by Westinghouse and Hays are paid (118, 119). As to the concealment of these assets, there can be no question as to lack of knowledge on the part of petitioning creditors prior to the four months period, because, as we have already shown, knowledge of these modifying contracts was not had until the answer herein was filed.

The most that can be said, in criticism of the lower court's findings and its order of adjudication, is that appellees plead the consideration set forth in the contract of February 27, 1930, and proved the concealment of the consideration of the two modifying contracts. In other words, that appellees have alleged the whole and proven only the part. We submit that, if that part was an asset concealed, there is still a concealment of assets clearly within the four months period. The Bankruptcy Act merely requires that an asset be concealed. It does not specify what the value of that asset shall be, and we submit that, having pleaded that the asset was worth $75,000.00, there is no variance if appellees were able to prove only a lesser value than $75,000.00 by reason of later modifying contracts, the existence of which were not known at the time the petition was filed. If appellant's theory in this regard were correct, all that would be necessary for a fraudulent debtor to evade an adjudication in bankruptcy would be to wrongfully dispose of or reduce the value of the asset concealed, thus encouraging further fraud on creditors.

IV.

CONCLUSION.

In conclusion we submit:

1. That the lower court heard all of the testimony of all of the witnesses at the trial and had the opportunity to observe the demeanor of these witnesses on the stand. Its findings are therefore not subject to review, and should be accepted by this court, unless manifest error is shown.

2. That any one act of bankruptcy, if supported by the testimony, is sufficient to warrant the adjudication.

3. That the concealment, both of the bank account and the assets represented by the various contracts, have been definitely established.

4. That these concealments of assets continued to within four months of the filing of both the original and amended petitions, and it has not been established that petitioning creditors were charged with knowledge of such concealment prior to the four months period.

5. That neither destruction, change, or decrease in value of the concealed assets changed the status of the concealments.

6. That each and every one of the concealments proven were with the intent at least to hinder and delay creditors, and that the evidence warrants the further conclusion that they were with the intent to defraud creditors, although proof of fraud was not necessary to the adjudication.

7. That to deny an adjudication in bankruptcy in this case would be to aid, assist and comfort appellant and "The Unholy Three" in perpetuating their wrongdoing and to enable the latter to profit at the expense of the former's creditors, notwithstanding the fact that the lower court found that this entire case, and the transactions of Hays, Diehl and Wise, *are tainted with fraud and concealment and warrant a full and complete investigation through the processes of the bankruptcy court.*

Dated, San Francisco,
April 1, 1935.

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